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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 384

FORREST S. SMITH, TRUSTEE OF THE PROPERTY OF HOBOKEN MANUFACTURERS RAILROAD COMPANY, DEBTOR, ET AL.,

Petitioners,

vs.

HOBOKEN RAILROAD, WAREHOUSE AND STEAMSHIP CONNECTING COMPANY, AND HOBOKEN LAND AND IMPROVEMENT COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 384

FORREST S. SMITH, TRUSTEE OF THE PROPERTY OF HOBOKEN MANUFACTURERS RAILROAD COMPANY, DEBTOR; THE DEBTOR, HOBOKEN MANUFACTURERS RAILROAD COMPANY; AND SEATRAIN LINES, INC., A CREDITOR,

Petitioners,

vs.

HOBOKEN RAILROAD, WAREHOUSE AND STEAMSHIP CONNECTING COMPANY, AND HOBOKEN LAND AND IMPROVEMENT COMPANY,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

To the Honorable Chief Justice and the Associate Justices of the Supreme Court of the United States:

Petitioners, Forrest S. Smith, Trustee of the property of Hoboken Manufacturers Railroad Company, Debtor; the debtor Hoboken Manufacturers Railroad Company; and Seatrain Lines, Inc., Stockholder and a Creditor of the

Debtor, respectfully present this petition for a writ of certiorari to review the final decision of the United States Circuit Court of Appeals for the Third Circuit, rendered and filed July 17, 1945, which affirms Order No. 39 of the United States District Court for the District of New Jersey in proceedings under Section 77 of the Bankruptcy Act (Title 11, U. S. Code, Section 205) for the reorganization of the Hoboken Manufacturers Railroad Company.

Summary and Short Statement of the Matter Involved

Hoboken Manufacturers Railroad Company (herein generally referred to as the Debtor or Lessee) is a New Jersey corporation operating a switching railroad line to New York Harbor waterfront in Hoboken, New Jersey. It is a common carrier engaged almost exclusively in the transportation of freight in interstate and foreign commerce subject to the provisions of the Interstate Commerce Act (U. S. Code, Title 49). Its line of railroad connects on the north with the line of the Erie Railroad and through this connection and a float bridge it interchanges freight with other trunk line railroads serving New York Harbor (R. 15a). It serves the piers of numerous steamship lines and the plants of important industries along the New Jersey waterfront.

Seatrain Lines, Inc. (hereinafter referred to as Seatrain) owns all of the stock of Hoboken Manufacturers Railroad Company, Debtor, except directors' qualifying shares, is a very substantial Creditor of Debtor, and is itself a common carrier by water, party to through routes with Debtor, and as such interested in its continued operation.

On July 26, 1943, Hoboken Manufacturers Railroad Company filed a petition for reorganization under Section 77 of the Bankruptcy Act (U. S. Code, Title 11, Section 205)

in the United States District Court for the District of New Jersey (R. 15a). On the same day said Court made its Order No. 1 approving the petition, continuing the Debtor in possession of its property and restraining all persons from taking any action to interfere with such possession or with the continued operation of the railroad (R. 23a ff).

By Order No. 5 entered on October 11, 1943, the Court appointed Forrest S. Smith, Trustee of the Debtor (R. 35a ff). The Interstate Commerce Commission approved this appointment by its Order of November 4, 1943 (R. 38a), and the Trustee duly qualified by filing his approved bond and oath on November 12, 1943, and thereupon, by direction of the Court, entered into possession of the debtor's property.

The major part of debtor's right of way and line of railroad is held by it under a ninety-nine year lease dated June 19, 1906, from Hoboken Railroad Warehouse and Steamship Connecting Company (hereinafter referred to as the "Connecting Company"), (Ex. D-1, R. 82a ff). Two additional pieces of land known respectively as Plots A and B are held under ninety-nine year leases likewise dated June 19, 1906 from Hoboken Land and Improvement Company (hereinafter referred to as the "Improvement Company"), the parent corporation of the Connecting Company (R. 61a ff). By a "tie-in" indenture dated January 19, 1913, the Debtor agreed that said leases of Plot A and Plot B should terminate on the expiration or earlier termination of the Connecting Company lease. The Debtor also owned in fee other parcels of land which were small but vital for the operation of the railroad.

The lease from the Connecting Company (Ex. D-1, R. 82a ff) contained a covenant whereby the Debtor agreed that it would not sell or transfer the lease or underlet the de-

mised premises without the previous consent of the lessor and provided, further, that:

> "this covenant shall also apply to any unauthorized sale or transfer thereof or underletting of the demised premises, or any part thereof, or of the said rights and privileges, or any of them, whether made by the lessee in any proceeding, whether at law or in equity or otherwise, to which the lessee may be a party, whereby any of the rights, duties and obligations of the lessee shall or may be transferred, encumbered, abrogated or in any manner altered without the consent of the lessor first had and obtained * * *."

There was no express reference to bankruptcy, to a petition in bankruptcy or to a petition for reorganization. The lease provided that if the lessee (the Debtor) should fail to observe any covenant of the lease and the default should continue for "thirty days after notice from the Lessor of such default and requiring the Lessee to remedy the same", the Lessor, the Connecting Company, at its option, might give notice to terminate the lease (R. 43a, 44a).

On February 8, 1944, the Connecting Company noticed a motion and filed a petition in the District Court (R. 41a ff) praying for an order modifying the restraints in Order No. 1 (R. 23a, 33a) and Order No. 5 (R. 35a) to permit it to serve written notice upon the Debtor of the termination of its lease, claiming that the qualification of the Trustee and his entering into possession of the Debtor's property, pursuant to the Court's order, constituted a breach by the Debtor of the aforesaid covenant (R. 40a-46a). The motion was argued before Judge Fake on February 14, 1944, and briefs were thereafter submitted.

Meanwhile the Debtor had sought and had from time to time been granted by the District Court additional time within which to file a plan of reorganization. The Trustee on May 26, 1944, noticed a motion and filed a petition in

the District Court (R. 48a ff) reciting the circumstances that then prevented determination as to whether it would ultimately be for the benefit of Debtor's estate and its creditors for executory contracts to be adopted or to be rejected, and praying that, because executory contracts adopted by the Trustee may be rejected in any plan of reorganization, while executory contracts, if rejected by the Trustee, would not be available in a plan of reorganization, he be instructed to elect to continue in force and adopt all executory contracts, including the leases above described. Judge Fake, by Order No. 27 (R. 51a) directed the Trustee to adopt and continue in force any and all executory leases and contracts to which the Debtor was a party, including the leases of June 19, 1906. No appeal from this order was taken by any party. Notice of adoption of such leases, pursuant to the order, was given by the Trustee to the Connecting Company and the Improvement Company (R. 52a and 53a).

Thereafter, on August 4, 1944, Judge Fake filed his opinion (R. 55a ff). Although he had directed the Trustee to adopt and continue the leases in effect, he nevertheless found that the covenant against unauthorized transfer in the main stem lease had been previously breached by the qualification of the Trustee and his entry into possession of the Debtor's property. He ruled "that since the Debtor-lessee's title passed to the Trustee prior to the adoption, nothing was gained or lost by the adoption insofar as present issues are involved (R. 59a)". He therefore granted the Connecting Company's motion to terminate the lease "to take effect upon production to the Court of conclusive evidence that the requirements of the laws relating to the continuous operation of the railroad have been complied with".

This last phrase of Judge Fake's opinion had reference, among other things, to the provisions of Section 1 (18)

the Interstate Commerce Act (U. S. Code, Title 49) prohibiting any party from acquiring or operating a railroad in interstate commerce without having first obtained from the Interstate Commerce Commission a certificate that the present or future public convenience and necessity require or will require the operation of such railroad. Neither the Connecting Company nor the Improvement Company had obtained such a certificate. The Connecting Company thereafter filed with the Interstate Commerce Commission a petition for the issuance to it of a certificate of convenience and necessity under Section 1 (18), but by Order dated December 2, 1944, the Interstate Commerce Commission dismissed the application holding that the Connecting Company was not required to hold such a certificate in order lawfully to reacquire and operate the railroad (R. 66a-75a).

On December 19, 1944, the District Court entered its Order No. 39 (R. 76 (a) ff) which, after reciting that the Court was satisfied (presumably by the decision of the Commission) "that the requirements of the laws relating to the continuous operation of the railroad have been complied with" authorized and empowered the Connecting Company to serve written notice upon the Debtor and Trustee of the termination of the main-stem lease for breach of the covenant against assignment and to terminate the leases of Plots A and B under the tie-in agreement, and to enter the demised premises, including all additional property acquired by the lessee during the lease, and thenceforth to hold, possess and enjoy the same free from any right of the Debtor or Trustee to use the demised premises for any purposes whatsoever. The District Court's order also directed the Trustee to deliver to the Connecting Company "all property of the debtor in the possession or under the control of the Trustee and presently held or used for railroad purposes, whether real, personal or mixed", excepting money, cash, accounts receivable, choses in action

or other intangible claims "notwithstanding conflicting claims thereto" (R. 77a).

The Circuit Court of Appeals, in an opinion filed July 17, 1945, affirmed this order. It did so, however, not upon the ground that the qualification of the Trustee was a breach of the covenant against transfer, but upon the ground "that the lease was breached when it was adopted by the Trustee" (which adoption was made only pursuant to the order and direction of the District Court). Notwithstanding that no plan for the reorganization had yet been presented which would indicate the disposition to be made of its property, the Circuit Court of Appeals upheld the direction of the District Court that the Trustee turn over to the Connecting Company all the property of the Debtor, including two small parcels owned in fee and property concerning which there were conflicting claims, on the ground that this would permit "the operation of this small trackage as a part of the main stem of the railroad and in addition provides means whereby the contested claims may be disposed of promptly".

It is this decision of the Circuit Court of Appeals, affirming Order No. 39 of the District Court, of which your petitioners seek a review.

Jurisdictional Statement

The jurisdiction of this Court is invoked under United States Code, Title 28, Section 347 (Judicial Code, Section 240 (a) as amended). The decision of the Circuit Court of Appeals, of which review is sought, was entered July 17, 1945.

Questions Presented

1. Did the qualification of the Trustee, appointed by the Court in a proceeding for the reorganization of Debtor railroad under Section 77 of the Bankruptcy Act or the subsequent adoption of the main stem lease by the Trustee,

pursuant to the order of the Court, for the purpose of fulfilling the Debtor's obligations thereunder, including the payment of rent, and of conserving the lease and the railroad's property in order to make possible the preparation, submission and carrying out of a plan of reorganization in which the Debtor might continue the lease, constitute a breach by the Debtor lessee of the covenant in the lease against unauthorized transfer?

2. In the proceeding under Section 77 of the Bankruptcy Act, did the qualification of the Trustee or the adoption of the main stem lease by the Trustee, pursuant to the order of the District Court, entitle the Connecting Company, landlord, to terminate the lease and have the property returned to it for breach of the covenant against transfer, thereby frustrating the reorganization of the Debtor as a railroad, for the purpose of which the proceeding was instituted?

3. If the qualification of the Trustee or the adoption of the lease by the Trustee constituted a breach of the covenant in the lease against transfer, was the covenant contrary to public policy and unenforceable?

4. Did the District Court err in holding that the qualification of the Trustee in the proceeding under Section 77 for the reorganization of Debtor railroad, or the adoption of the lease by the Trustee, entitled the landlord to terminate the lease for breach of the covenant against unauthorized transfer?

5. Did the Circuit Court of Appeals err in holding that the adoption of the lease by the Trustee, pursuant to the order of the Court in the proceeding for the reorganization of Debtor railroad under Section 77 entitled the landlord to terminate the lease for breach of the covenant against unauthorized transfer?

6. Prior to the submission and consideration of a plan of reorganization under Section 77 of the Bankruptcy Act, was the termination of the main stem lease premature?

7. Did the District Court err in ordering the Trustee to deliver to the Connecting Company not only the property covered by the main stem lease and the tie-in agreement, but also all other property of the Debtor held by the Trustee, except money and intangibles, including property owned in fee by the Debtor and property as to which there were conflicting claims, in order that the Connecting Company might operate these properties as a railroad?

8. Even if the Connecting Company was entitled to terminate the main stem lease and take back the properties covered thereby and by the tie-in agreement, did the District Court, in advance of a plan or reorganization, have discretion to direct the delivery to the Connecting Company of other property owned by the Debtor?

9. Did the District Court err in accepting the decision of the Interstate Commerce Commission that the Connecting Company, landlord, was not required to secure a certificate of convenience and necessity under Section 1 (18) of the Interstate Commerce Act in order lawfully to reacquire and operate the leased premises as a railroad in interstate commerce as conclusive evidence that the requirements of the laws relating to the continuous operation of the railroad have been complied with?

10. Did the District Court err in permitting the Trustee to surrender the lease and discontinue the operation of the railroad without prior approval by the Interstate Commerce Commission authorizing such discontinuance of operations?

Reasons Relied On for the Allowance of the Writ

The questions presented are of great concern to petitioners, for if the order of the District Court was proper, terminating the leases and turning all of the Debtor's property over to the Connecting Company, the reorganization of the Debtor as a railroad is completely frustrated, the Debtor ceases to be an operating railroad and the creditors of the Debtor lose all access not only to the leased properties but to other properties owned by the Debtor.

It is believed that these questions are also of great general importance in connection with the administration of Section 77 of the Bankruptcy Act and the reorganization of railroads thereunder. It is well known that a large part of the railroad mileage of the country is held by the operating companies under long-term leases. At the time, years ago, when such leases were executed, covenants against assignment in general terms were usual. The entire theory of reorganization, to carry out which Section 77 of the Bankruptcy Act was adopted, has been developed since such leases, including that here involved, were executed. Although covenants against transfer, such as that in the present lease, may contain references to transfers accomplished by court order, their obvious intention was to protect landlords from having strangers substituted without their consent for the tenants with whom they contracted. The whole purpose of a reorganization under Section 77, however, is to avoid distribution of a debtor's assets, to keep the railroad properties together for continued operation after reorganization, and to enable the Debtor itself to carry on. *Van Schaick* v. *McCarthy*, 116 F. (2d) 987 (C. C. A. Tenth). It is only if a lease is rejected that the Debtor lessee does not continue the lease, and in that event the property goes back to the landlord by virtue of the rejection.

If such a covenant against transfer as that here gives a landlord of railroad properties the right to terminate a lease, railroad reorganizations will in large part be made difficult, if not sometimes impossible.

It has been said by this Court that "Sec. 77 manifest the intention of Congress to place reorganization under the leadership of the Commission, subject to a degree of participation by the court." *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448. This intention would be defeated because the railroad properties would be dissipated, as here, before any plan could come before the Commission for its consideration.

Under the circumstances the questions involved are of far reaching importance. They include the effect to be given to such covenant against transfer in leases of railroad properties; whether with the enactment of Section 77 covenants which would permit termination of leases under circumstances such as those here became contrary to public policy; whether it is consistent with the provision of Section 77 (Title 11, Section 205) within the meaning of paragraph (1) thereof, that a clause permitting termination of a lease of railroad property shall be enforceable as provided in Section 110 (b). None of these questions has been passed upon by this Court.

Moreover, the order of the District Court rests on the premise that a landlord is not required by Section 1 (18) of the Interstate Commerce Act to obtain a certificate of convenience and necessity from the Commission in order lawfully to operate railroad property recovered by termination of a lease, although it has not itself operated as a railroad since Section 1 (18) was enacted. It is submitted that this premise is erroneous, and that the question presented is one of broad concern in connection with leases of railroad properties and their reorganization.

It is believed that these questions and other issues involved herein are of such moment that this Court should grant certiorari to review the decision of the Court below.

WHEREFORE, your petitioners respectfully pray that Writ of Certiorari issue to the United States Circuit Court of Appeals for the Third Circuit and submit herewith their brief in support of this petition.

Respectfully submitted,

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Dated: August 30th, 1945.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 384

FORREST S. SMITH, TRUSTEE OF THE PROPERTY OF HOBOKEN MANUFACTURERS RAILROAD COMPANY, DEBTOR; THE DEBTOR, HOBOKEN MANUFACTURERS RAILROAD COMPANY; AND SEATRAIN LINES, INC., A CREDITOR, *Petitioners,*

vs.

HOBOKEN RAILROAD WAREHOUSE AND STEAMSHIP CONNECTING COMPANY, AND HOBOKEN LAND AND IMPROVEMENT COMPANY, *Respondents.*

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

Preliminary Statement

We refer to the foregoing petition for a summary statement of the matter involved and the jurisdictional statement. The opinion of Judge Fake in the District Court is reported in 56 Fed. Supp. 187 and printed in R. 55a. The opinion in the Circuit Court of Appeals is not yet reported but is printed in R. 116.

Argument

Point I

Neither Filing of the Section 77 Reorganization Petition, Nor Qualification of the Trustee, Nor His Adoption of the Leases Pursuant to Direction of the Court, Entitles the Landlord to Terminate the Main Stem Lease on the Ground of Breach by the Debtor of the Covenant Against Assignment.

This point covers numbers 1 to 5 of "The Questions Presented" in the petition.

Sub-division (d) of Section 77 of the Bankruptcy Act provides that the Debtor, after a petition for reorganization is filed:

> "shall file a plan of reorganization within six months of the entry of the order by the judge approving the petition as properly filed * * * unless such time is extended by the judge from time to time for cause shown."

Sub-division (b) provides:

> "A plan of reorganization within the meaning of this section * * * may reject contracts of the debtor which are executory in whole or in part, including unexpired leases; * * *."
>
> * * * * * * *
>
> "The adoption of an executory contract or unexpired lease by the trustee or trustees of a debtor shall not preclude a rejection of such contract or lease in a plan or reorganization approved hereunder, * * *."

By the same sub-division, it is specifically provided that:

> "In case an executory contract or unexpired lease of property shall be rejected, or shall not have been adopted by a trustee appointed under this section, * * * or shall be rejected by any plan, any person

> injured by such non-adoption or rejection shall * * * be deemed to be a creditor of the debtor to the extent of the actual damage or injury determined in accordance with principles obtaining in equity proceedings."

and that:

> "The running of all statutes of limitation shall be suspended during the pendency of a proceeding under this section."

By sub-division (c) (2), it is provided:

> "Prior to the appointment of a trustee, the debtor on behalf of the court shall continue in the possession of the property and shall operate the business thereof during such period, and shall have all the title to the property and shall exercise all power consistent with the provisions of this section, subject at all times to the control of the judge, and to such limitations, restrictions, terms, and conditions as he may from time to time impose and prescribe."

and that the trustee appointed by the court upon filing bond

> "shall have all the title and shall exercise, subject to the control of the judge and consistently with the provisions of this section, all of the powers of a trustee appointed pursuant to section 72 or any other section of this title, * * * and, subject to the control of the judge and the jurisdiction of the Commission * * * the power to operate the business of the debtor."

From these provisions of the statute, two points emerge: first, that the Court and the trustee take possession and operate the property, not under the terms of the lease, but pursuant to the statute; and second, that the statute contemplates that a reasonable period is allowed to reject or adopt a lease, but if adopted it may later be rejected under the plan of reorganization.

Probably the principal decision on the question here involved, which squarely supports the foregoing points, is that of Judge Learned Hand for the Circuit Court of Appeals for the Second Circuit in *Palmer* v. *Palmer* (C. C. A. Second, 1939), 104 F. (2d) 161, Cert. denied 308 U. S. 590, cited with approval in *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523. *Palmer* v. *Palmer* involved a phase of the New Haven Reorganization. Judge Hand said (page 163):

> "A lease, being property *cum onere*, does not pass *to a trustee in bankruptcy*, unless he adopts it."

He remarked that if the question were to arise for the first time it might be difficult to see

> "by what power the court could keep a trustee in possession while he was determining his course, without compelling him meanwhile to fulfill the conditions imposed upon the term, for instance, the payment of any rent, secured by a right of reentry."

But he went on to say, however:

> "Nevertheless, the contrary has been generally held: and the trustee's adoption of the term is said to 'relate back' to the beginning of the proceeding, or at least to adjudication. The reason for this is not clear. It does not follow from Sec. 70 of the Bankruptcy Act, 11 U. S. C. A. Sec. 110, which vests the trustee's title only 'by operation of law'; for title to the term vests, not by operation of law at all, but only by the trustee's adoption. Be that as it may, the trustee need not pay the rent during the probationary period, and the court will hold off the lessor, and force him to be content with the value of the use and occupation meanwhile, though ordinarily it will fix that at the same amount as the rent. This was the result in Quincy, etc., R. Co. v. Humphreys, 145 U. S. 82, 12 S. Ct. 787, 36 L. Ed. 632, and in United States Trust Co. v. Wabash Rail-

way, 150 U. S. 287, 14 S. Ct. 86, 37 L. Ed. 1085; though so many other circumstances were thought relevant that we are not clear as to the precise scope of either ruling. But we have ourselves a number of times declared that the trustee's title 'relates back,' or that he is liable only for use and occupation, and in some instances what we said was necessary to the result. In Re Frazin, supra, 183 F. 28, 32; In re Sherwoods, 2 Cir., 210 F. 754, Ann. Cas. 1916A, 940; Johnson v. Emerson Phonograph Co., 2 Cir., 296 F. 42, 45; Heineman Corp. v. Levy & Co., 2 Cir., 6 F. 2d 970, 975; In re United Cigar Stores Co., 2 Cir., 69 F. 2d 513, 515; Central Manhattan Properties v. D. A. Schulte, 2 Cir., 91 F. 2d 728, 730. Whether justified in principle of not, the doctrine has by now become too well fixed to be uprooted, especially since no change was made when the whole subject was overhauled in the Chandler Act."

The Connecting Company lease does not contain a "bankruptcy" clause expressly providing that in the event of the filing of a petition in bankruptcy or insolvency the lease shall terminate. Nor does it provide for termination if the lessee should seek the benefits of a railroad reorganization act in its own interest and that of the public. The covenant is solely against selling, assigning or transferring. It provides that the landlord's right to terminate the lease,

> "shall also apply to any unauthorized sale or transfer * * * whether made by the lessee or in any proceeding, whether at law or in equity or otherwise, to which the Lessee may be a party, whereby any of the rights, duties and obligations of the Lessee shall or may be transferred, encumbered, abrogated, or in any manner altered. * * *"

It is well settled that provisions for forfeiture of leases are to be strictly construed. They must be construed strictly, not only in accordance with their own language

but also in the light of the provisions and purposes of applicable statutes. It has accordingly been held that a covenant not to assign or transfer is not breached by a petition in bankruptcy so as to permit the landlord to assert a forfeiture. Only if the lease specifically and in express terms provides that it shall terminate upon bankruptcy is it held that bankruptcy works a forfeiture.

In re *Prudential Lithograph Co.* (D. S. N. Y.), 265 Fed. 869; aff'd 270 Fed. 469; cert. den. 256 U. S. 692;
In re *Levinson*, 295 Fed. 146 (D. C. W. D. Wash. N. D. 1923);
In re *Gutman*, 197 Fed. 472;
Gazlay v. *Williams*, 210 U. S. 41.

In the *Levinson* case, *supra*, the lease provided as follows:

> "It is expressly agreed that if default be made in the payment of rent above reserved or any part thereof, or any of the covenants by the tenant, it shall be lawful for the owners and their lawful representatives at any time thereafter, without notice, to declare said term ended and to re-enter said premises with or without process of law * * * and * * * repossess and enjoy as before this lease."

In respect to the right of the lessor to repossess the property on the theory that there was an assignment because the lessee became bankrupt, the Court said:

> "There is no express penalty fixed by the terms of the lease against assignment thereof, the provision being in the nature of a covenant, and not a conditional limitation of the estate, which would end by determination of the grant, whereas the covenant requires reentry to terminate the estate. Hague v. Ahrens, 53 Fed. 58, 3 C. C. A. 426. No words of agreement will create a condition. To produce this effect apt terms must be employed. Den v. Post, 25 N. J. Law, 285.

No apt words being used for reentry because of assignment, the phrase 'any of the covenants by the tenant,' under the rule ejusdem generis, would refer to *default in the payment of rent*, and since covenants against assignment of a lease are not favored (270 Fed. 469, supra), but construed with great jealousy (Riggs v. Purcell, et al., 66 N. Y. 193), and the provisions for the forfeiture of a lease being always construed strictly as against the lessor to prevent, rather than aid forfeiture (Camp v. Scott, 47 Conn. 366-375), there appears to be no legal inhibition against this assignment."

In *Gazlay* v. *Williams*, 210 U. S. 41, the facts were as follows:

Under a written agreement, "G" leased to "K" for a period of years certain premises. The lease contained a provision to the effect that if "K," the lessee, should assign the lease or underlet the premises or if lessee's interest should be sold under execution of other legal process without the written consent of lessor, or if lessee should fail to keep any of the other covenants of the lease, lessor should have the right to re-enter the premises and repossess them and thereupon the lease would become void and terminate. During the existence of the lease the lessor "G" filed a petition in an Ohio court against "K" for recovery of rent due under the lease and also asked that the receiver be appointed to take charge of all the property of "K," including the leasehold estate, and that the unexpired term of the lease be sold subject to all the terms and conditions contained in the lease. Thereafter, with the consent of the lessor, the leasehold was purchased by "B." "G" did not give its written consent to the sale of the leasehold to "B" but nevertheless acquiesced in it, and the Court said that the resulting agreement between "B" and "G" could be considered as if "B" were the original lessee (p. 48).

Thereafter, "B" was adjudged a bankrupt and "W" was appointed trustee of his property, including the leasehold estate. Thereafter "W" filed an application for the sale of the leasehold, making the lessor a party thereto and asking that they be required to set up any claim that they might have. It was apparently the purpose of the trustee in filing the foregoing application to have the Court determine whether the covenants described and the lessor's right of re-entry would constitute a cloud upon the leasehold in the event it was sold by him.

The Court held that the transfer of the property to "W," the trustee, was effected by operation of law and did not constitute a breach of the covenant of the lease giving the lessor a right of re-entry. The Court further held that the sale by "W" for the benefit of Brown's creditors was not forbidden by the condition of the lease and would not be a breach thereof because it would not be a voluntary assignment by the lessee nor a sale of the lessee's interest but of the trustee's interest arising under the bankruptcy proceedings.

In *In re Prudential Lithograph Co., supra*, the lease under consideration contained covenants similar to those contained in our Debtor's lease. It provided that the lease should not be assigned nor the premises underlet without the written consent of the lessor endorsed thereon and also contained provisions that "in case the rent was behind and unpaid or in case of the violation of any of the covenants, conditions or agreements contained therein, the lease, at the option of the lessor, should become null and void." The lessee having become a bankrupt, the lessor elected to terminate the lease on the ground that an assignment had been made by operation of law. The Court held (p. 473):

> "a covenant against an assignment of a lease can be so drawn as to provide for a forfeiture by an assign-

ment by operation of law but there is no such express provision in the lease before the court and in its absence a court will not infer one."

Applying the principle of these cases, we submit that only if it were expressly provided in a lease of a railroad that it should be forfeited if proceedings for reorganization should be instituted under Section 77 could it be argued that in such an event the landlord would be entitled to terminate the lease. Even if a lease contains such a provision in express terms, we submit that it should be held unenforceable as against public policy. There is no provision in the lease involved here which can be said to constitute an express provision for termination in the present circumstances.

Looking at the covenant in the lease, Article Third, paragraph (1), it is plain that neither the inauguration of the reorganization proceedings, the qualification of the Trustee nor the adoption of the lease, subject to its rejection in the plan of reorganization, by the Trustee violated the first part of the paragraph, whereby it was provided that:

> "The Lessee shall not and will not sell, assign or transfer this lease or underlet the demised premises. * * *"

So far this is a typical covenant against assignment and the cases previously cited are conclusive that such a clause does not afford a right to terminate upon bankruptcy, much less because of what is done in a reorganization proceeding.

The Landlord's claim rests, therefore, on the last sentence of the paragraph, that

> "This covenant shall also apply to any unauthorized sale or transfer thereof or underletting of the demised premises, or any part thereof, * * * whether made by the Lessee or in any proceeding, whether at law or in equity or otherwise, to which the Lessee may

be a party, whereby any of the rights, duties and obligations of the Lessee shall or may be transferred, encumbered, abrogated or in any manner altered, without the consent of the Lessor * * *."

In the first place, what is meant by an "unauthorized" transfer? Certainly the procedure provided by statute to enable a railroad to continue in operation in the service of the public cannot be regarded as "unauthorized."

Obviously, the adoption of the lease by the Trustee is neither a "sale" nor an "underletting" of the demised premises. If it is described at all by the language of the lease, it is as a "transfer." But not all transfers are barred by the covenant: It is only a transfer by which "The rights, duties, and obligations of the Lessee shall or may be transferred, encumbered, abrogated or in any manner altered" which are within the prohibition of the covenant. This makes it necessary to consider what really takes place when a lease of a railroad is adopted by a Trustee in a reorganization proceeding.

A trustee in an ordinary bankruptcy proceeding takes the debtor's property for the purpose of liquidating it for the benefit of creditors. The expectation is that the assets will be sold and the bankrupt's title to and interest therein will be extinguished. This is plainly what was contemplated by the language of the lease involved here. In the reorganization of a railroad under Section 77, however, although the statute in Subsection (c)(2) says that "The trustee * * * shall have all the title * * * of a trustee appointed pursuant to section 72," this is subject to the proviso that he may exercise his powers only "subject to the control of the judge and consistently with the provisions of this section." And even the authority of the judge is limited. The trustee may not sell the leasehold or any other asset, nor may the judge direct him to do so.

The property may ultimately be disposed of only in accordance with a plan of reorganization approved by the Interstate Commerce Commission and then confirmed by the court. The only exception to this is the right of a trustee to reject executory contracts. The trustee holds the debtor's property, not for the sake of disposing of it, but for the purpose of keeping it intact as a going railroad and of returning it to the debtor when a plan for reorganizing the debtor's obligations and capital structure has been worked out. In other words, upon adoption of the lease and until a plan of reorganization becomes effective the trustee really holds the property for the debtor; he pays the debtor's obligations under the lease from the debtor's funds and, in effect, for the debtor's account. And unless the plan of reorganization provides for the rejection, as provided for under subsection (b) of Section 77, or modification of the lease, the debtor or lessee resumes all of its rights and obligations thereunder for itself.

In short, we submit that what transpires when a trustee in a railroad reorganization adopts a lease is not a transfer of the sort described by the covenant involved here, in that it does not permanently transfer nor does it of itself encumber, abrogate or alter the rights, duties and obligations of the lessee. It preserves them.

If a corporation worked out a reorganization of its capital structure by agreement among its security holders and continued to carry out the terms of any lease or executory contract which it might have, it could not be claimed that there was a transfer or assignment of a lease which would constitute a breach of a covenant against assignment. The tenancy would be uninterrupted. This is exactly the result here if a lease is adopted. The reorganization is carried on under the supervision of the court and the Interstate Commerce Commission instead of by voluntary

agreement among the security holders and creditors, but it is nevertheless a reorganization and not a liquidation or distribution and transfer of assets. The Trustee's function is to preserve the debtor's estate during the accomplishment of reorganization and carry out all of the terms of the lease on behalf of the debtor. When the plan of reorganization is worked out and the reorganization completed, if the plan provides for the adoption of the lease by the debtor there will, in effect, have been no interruption whatever in the debtor's occupancy of the premises and performance of the terms of the lease. It is only if the lease should ultimately be rejected that there would be any transfer of the lease or leased premises from the lessee-debtor and this would be a transfer to the landlord. Hence, it follows that with the adoption of the lease by the Trustee, pursuant to the order of the court, it becomes premature to assert that there has been a breach of the lease entitling the landlord to re-enter, and whether such a contention may ultimately be made can only be determined after a plan of reorganization has been submitted.

It may be observed, moreover, that a contrary conclusion would produce the anomalous result that the lower court, by its own act in directing the trustee to adopt the lease, would be the cause of a termination of the lease by the landlord, which would defeat the very adoption by the Trustee which the Court directed. If this were the law the lower court should not have directed the adoption of the lease but should, as he had the right to do, have allowed the matter of rejection or adoption to await the submission of a plan of reorganization, in which event, in accordance with the authorities cited under Point I, all rights of the landlord under the lease would have been held in suspense.

Moreover, we submit that it cannot be said that the adoption of the lease by the Trustee was "without the consent of the Lessor." This contention is not available to

the landlord because the statute itself provides the consent. Any other view would mean that a landlord could prevent the reorganization of a railroad and cause its dismemberment by refusing consent to a reorganization provided for by statute. Here, again, it is essential to appreciate the difference between the adoption of a lease by a trustee in the reorganization of a railroad and the taking over by a trustee in bankruptcy of the assets of a bankrupt for the purpose of sale. It is not inconsistent with public policy for a lessor to object to the sale of a leasehold to a total stranger. It would defeat the reorganization machinery provided by the Congress to keep railroads functioning if a lessor could be heard to assert a refusal to allow a trustee to adopt a lease for the purpose of preserving the property and operating it until a plan of reorganization is worked out and then of returning it to the debtor, or of rejecting it so that it will revert to the landlord. And a landlord leasing a railroad, even in 1906, had notice of the public interest in such property. The "Act to Regulate Commerce" was approved February 4, 1887, and after many amendments became the "Interstate Commerce Act" in 1920.

The Circuit Court adverted to the recent decision of this Court in *Finn* v. *Meighan*, 65 S. Ct. U. S. 1147, but recognized that the pertinent provision of the lease there being construed specified the filing of a "petition in bankruptcy." Furthermore, Section 77 of the Bankruptcy Act is independent of and differs radically in purpose from the part of the statute relating to ordinary bankruptcy proceedings and from Chapter X relating to corporate reorganizations. *Finn* v. *Meighan*, *supra*, makes it clear that Section 70 relating to ordinary bankruptcy and providing as to leases that "an express covenant that an assignment by operation of law or the bankruptcy of a specified party thereto shall terminate the lease or give the other party an

election to terminate the same shall be enforceable" applies also to Chapter X reorganizations by virtue of Section 102 of that chapter specifically incorporating Chapter VII, which includes Section 70 therein. There is no similar provision specifically incorporating Section 70 of the Bankruptcy Act in Section 77 relating to railroad reorganizations.

Petitioners submit, therefore, that qualification of the Trustee under Section 77—he then taking the leasehold estates "*cum onere*"—and his subsequent limited adoption of the leases, subject to the statutory right to reject them in the plan of reorganization, did not breach the covenant against assignment in the Connecting Company lease, a strict construction of such forfeiture clause aided by public interest and policy as expressed in Section 77 favoring the Debtor and its reorganization.

Point II

The Purpose of Section 77 of the Bankruptcy Act is Reorganization of Railroads, Not Liquidation, so Termination of the Main Stem Lease, if Legal, Before Consideration of Any Reorganization Plan Is Premature.

In considering the primary question of the Connecting Company's right to terminate its lease, sight must not be lost of the nature of a reorganization proceeding under Section 77 of the Bankruptcy Act. In ordinary bankruptcy a trustee takes the bankrupt's property for the purpose of liquidating it in order that the assets may be realized upon for the benefit of the various creditors. The purpose of Section 77, however, is just the opposite. It is to keep the assets together, continue the corporation as a going railroad and rearrange its indebtedness, while so doing, in such a way as to enable the railroad to continue to function. Only such assets as constitute a drain upon the railroad, and

therefore defeat the purpose of continuing it in operation, are to be disposed of.

Thus, in *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, this Court said (p. 468):

> "These reorganizations require something more than contests between adversary interests to produce plans which are fair and in the public interest. When the public interest, as distinguished from private, bulks large in the problem, the solution is largely a function of the legislative and administrative agencies of government with their facilities and experience in investigating all aspects of the problem and appraising the general interest. Congress outlined the course reorganization is to follow. It established standards for administration and placed in the hands of the Commission the primary responsibility for the development of a suitable plan. When examined to learn the purpose of its enactment, Sec. 77 manifests this intention of Congress to place reorganization under the leadership of the Commission, subject to a degree of participation by the court.
>
> "It is clear from the discussions and the statute itself that there was recognition by everyone of the advantages of utilizing the facilities of the Commission for investigation into the many-sided problems of transportation service, finance and public interest involved in even minor railroad reorganizations and utilizing the Commission's experience in these fields for the appraisals of values and the development of a plan of reorganization, fair to the public, creditors and stockholders. The resulting legislation was an attempted balance between the power of the Commission and that of the court."

In *Continental Bank* v. *Rock Island Ry.*, 294 U. S. 648, this Court held that the Bankruptcy Court acting under the provisions of Section 77, although it could not impair, could nevertheless delay by injunction the enforcement of a contract which empowered the Continental Bank and other

lenders to sell collateral pledged as security for loans made to the debtor, on failure to pay interest, insolvency of the debtor or the appointment of a receiver for its properities. At pages 676 and 677 this Court said:

> "The injunction does not infringe Sec. 67 (d), U. S. C. Title 11, Sec. 107 (d). The substance of that provision is that bona fide liens shall not be affected by anything contained in the Bankruptcy Act. The injunction here in no way impairs the lien, or disturbs the preferred rank of the pledgees. It does no more than suspend the enforcement of the lien by a sale of the collateral pending further action. It may be, as suggested, that during the period of restraint the collateral will decline in value; but the same may be said in respect of an injunction against the sale of real estate upon foreclosure of a mortgage; and such an injunction may issue in an ordinary proceeding in bankruptcy. *Straton* v. *New*, 283 U. S. 318, 321, and cases cited. A claim that injurious consequences will result to the pledgee or the mortgagee may not, of course, be disregarded by the district court; but it presents a question addressed not to the power of the court but to its discretion—a matter not subject to the interference of an appellate court unless such discretion be improvidently exercised. So far as constitutional power is concerned, there is no difference between an injunction restraining the enforcement of a real-estate mortgage and one restraining the enforcement of a pledge by the sale of collateral security. Such differences as exist affect not the power but the propriety of its exercise—that is to say, the discretion of the court. Such an injunction, as just indicated, is within the contemplation of Sec. 77, and we need not inquire whether it would be admissible under the act in force prior to the adoption of that section. Compare *Straton* v. *New*, *supra*. Nor does Sec. 57 (h), 11 U. S. C. Sec. 93 (h), also invoked by petitioners, have any pertinent application to the question under discussion in the light of the provisions, purpose and aid of Sec. 77."

See also *United States Trust Co. v. Wabash Ruy. Co.*, 150 U. S. 287, 299, 300.

In an illuminating article discussing at length various problems in connection with railroad reorganization under Section 77, *Railroad Leases and Reorganization*, 49 Yale Law Journal 1401, Professor Mack, citing the foregoing and other decisions, concludes (p. 1413) that for a trial period which

> "in modern reorganizations will and should be somewhat longer than that accorded under old equity practice" (p. 1414)

during which a trustee may determine whether to adopt or reject a lease,

> "The court may prevent the Lessor from retaking its properties for this period without payment of any rent whatever" (p. 1413).

In *Van Sciaick v. McCarthy*, 116 F. (2d) 987 (C. C. A. Tenth), Circuit Judge Phillips, speaking for the Court, stressed the point that the purpose of a reorganization under Section 77 was to keep the debtor corporation going and not divorce it from its property or its property from it. At pages 992 and 993, he said:

> "Sec. 77 has for its main purpose the rehabilitation of the debtor by a readjustment of its financial structure in the interest of the debtor and its creditors and security holders, under a fair and equitable plan of reorganization which shall so modify or alter the rights of both secured and unsecured creditors that the fixed charges shall be brought within the probable future earnings available for the payment thereof. During the process of reorganization it contemplates the continued corporate existence of the debtor under the control and supervision of the court.
>
> "It may be doubted that, in view of the objects and purposes of Sec. 77 and the means provided for their

accomplishment, a secured creditor is entitled during the pendency of the proceeding to have income sequestered and subjected to the lien of his mortgage. Sec. 77 does not contemplate sale and liquidation or the application of earnings to the payment of mortgage securities. On the contrary, it provides for a fair and equitable plan of reorganization and a just allocation of the securities of the reorganized company, taking into consideration not only the principal but the unpaid interest on mortgage obligations. But we prefer not to rest our decision on this narrow ground.

"Sec. 77 provides for the submission of the plan to the Interstate Commerce Commission, for a public hearing before the Commission, for a certification of the plan to the court, and for a hearing before the court. It further provides that if the judge does not approve the plan, he may refer it back to the Commission for further action. It is manifest that a considerable period of time must necessarily elapse before a satisfactory and proper plan can be worked out and receive the requisite approval. During that period the railroad company must be operated by the trustees under the supervision and control of the court in the public interest and for the protection of the private interests involved, and to that end such expenditures must be made as are reasonably necessary to preserve and protect those interests and maintain the integrity of the railroad, so that it may be turned over to the reorganized company as a going concern. Sec. 77 contemplates that the reorganized road shall be a living, not a dying, railroad enterprise. To permit the competitive position of the road to be lost during the period of reorganization would greatly endanger the future earnings upon which the plan is to be largely based and out of which the reduced fixed charges are to be paid."

And in *In re Central of Georgia Ry. Co.*, 48 F. Supp. 445 (D. C., S. D. Georgia), aff'd in 135 F. (2d) 52 (C. C. A. Fifth), the Court emphasized that the purpose of Section

77 was to keep the railroad properties together until a plan of reorganization could be worked out. It said (p. 449):

> "To permit the steamship line to be divorced from the railway at this time is tantamount to a dismemberment of the system. If I properly understand the philosophy of section 77 of the Bankruptcy Act as amended, 11 U. S. C. A. Sec. 205, under which these proceedings were taken, among other things, it was to prevent the disintegration of a railway by parceling out the mortgaged property in divisions or according to prior liens, and to preserve it as a unit of the national transportation system until reasonable opportunity has been furnished to develop and submit a plan of reorganization which will be fair and equitable to all of the interests concerned. If at the very time the trustee, his advisory committee, and the several bondholders' committees are attempting to develop such a plan they are met with the threat that the steamship company, regarded by many of them as an integral part of the system, is to be withdrawn and liquidated or operated independently of the railway, they will be denied what I consider a reasonable opportunity through negotiation to reorganize the system as a whole."

It is clear from the foregoing language of this Court in the *Western Pacific* case that nothing should be done by the Bankruptcy Court which will prevent the consideration by the Interstate Commerce Commission of a plan of reorganization.

Under these circumstances, we submit that while a trustee appointed by the Court under Section 77 takes title to a debtor's assets, he may not, like a trustee in bankruptcy, sell the assets which constitute the railroad's property, and without which it may not operate, nor may he be directed by the Court to do so. These assets, such as the lease of the railroad's right of way, to the extent that they are essential to the reorganization of the railroad, he must

hold for the purposes of a plan of reorganization. Even if he elects not to hold a lease, he may not sell it; he may only reject it.

With a large part of the railroad mileage of the country operated under lease, and with a covenant against assignment being common in leases, the Congress in enacting Section 77 could not have contemplated or intended that the machinery thereby set up to keep the railroad property together pending reorganization, namely, the appointment and qualification of a trustee and his adoption of leases subject to their rejection in the plan of reorganization, would or should be used to automatically defeat the entire purpose of reorganization by enabling landlords to retake different sections of railroad property and thereby effectively frustrate a reorganization.

The foregoing considerations also bear directly upon the interpretation and effect of the lease.

We submit, therefore, that even admitting for argument's sake that the District Court was correct in holding the Connecting Company had a legal right to terminate its lease, entry of the termination order before considering any reorganization plan was premature.

Point III

Order No. 39 Should Be Reversed Also Because It Transfers Possession of Certain Railroad Property, Claimed by the Trustee, to the Landlord Before Determination of Title Rights Thereto.

The Order under review provides in part that:

> "3. Notwithstanding conflicting claims thereto, within the time and in the manner set forth in this order all property of the debtor in the possession or under the control of the trustee and presently held or used for railroad purposes, whether real, personal or mixed, excepting money in bank, cash on hand, accounts receiv-

able, choses in action or other intangible claims, and the evidences thereof, shall be delivered to said Hoboken Railroad, Warehouse and Steamship Connecting Company by the trustee. The trustee, or any other claimant, may thereupon file a claim or claims with the Clerk of this court, after first serving a copy thereof upon said company or its attorneys, for recovery of such property or its value and reasonable compensation for the use thereof, which claims will thereupon be determined by this court through reference to a Master or otherwise." (77a).

The property of the Debtor to which the Trustee asserts a claim, even though it is now used for railroad purposes and so under the forfeiture clause of the Connecting Company lease (Sub-paragraph (b), 87a), might revert to that landlord on termination of its lease, includes land and tracks leading to the float bridge and a short portion at the end of the right of way with tracks and two sidings. The Trustee and Debtor maintain that by an Indenture dated June 29, 1927, the Connecting Company released these properties to the Debtor (71a).

Paragraph 3 of the Order was included therein, as was Paragraph 4 (77a) relating to records of the Debtor required for the continued and uninterrupted operation of the railroad, so that there would be no cessation of operations during wartime. However, we submit that possession of the entire railroad property should have been left in the Trustee, and so under control of the Court, at least until determination of title to the property in dispute. The landlords would not be harmed thereby, for, aside from a period of time before adoption of the leases when use and occupation was fixed and paid at the rental rates provided therein, the Trustee has paid or, he operating at a profit and being able to pay, attempted to pay, all rent reserved by said indentures.

Point IV

The District Court Erred In Failing To Require the Landlord To Obtain a Certificate of Convenience and Necessity Under Section 1 (18) of the Interstate Commerce Act As Conclusive Evidence That the Requirements of the Laws Relating To Continuous Operation of the Railroad Had Been Complied With.

The District Court in its decision granting the Connecting Company's motion to terminate the lease provided that such termination should "take effect upon production to the Court of *conclusive* evidence that the requirements of the laws relating to continuous operations of the railroad have been complied with".

This requirement of the District Court had reference, among other things, to the provisions of Section 1 (18) of the Interstate Commerce Act (U. S. C. A. Title 49), which provides that:

> "After ninety days after this paragraph takes effect *no* carrier by railroad * * * shall acquire or operate any line of railroad * * * unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the * * * operation * * *."

The Connecting Company, in order to satisfy the Court's requirement, thereafter filed with the Interstate Commerce Commission an application for the issuance to it of a certificate of convenience and necessity under Section 1 (18) authorizing it to resume operations, but accompanied its application with a reservation challenging the Commission's jurisdiction to require it to obtain a certificate. The Commission rendered its decision, in which it held that the Connecting Company, being the owner and lessor of the

line of railroad in question, was under no obligation as a matter of law to obtain a certificate of convenience and necessity and accordingly, by its Order of December 2, 1944, dismissed the application.

This decision of the Commission cannot be reconciled with the provisions of Section 1 (18) (U. S. C. A. Title 49) or with its previous decisions and those of this Court. The provisions of Section 1 (18) that no carrier by railroad shall operate any line of railroad unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the operation of such line of railroad is all-inclusive and plainly does not contain any exception that would permit lessors to resume operations without first obtaining a certificate.

Prior to its decision in this matter the Commission had, in a number of cases, held that ownership of a line of railroad, even where the railroad had been in operation in interstate commerce, does not give the owner the right to operate the railroad. Under these decisions it is held that unless the owner was operating the railroad in question when Sec 1 (18) was enacted, it must obtain a certificate before it may lawfully operate it in interstate commerce. *Acquisition of Line By B. & H. S. R. R. Co.*, 90 I. C. C. 448, 453; *Missouri & A. Ry. Co., Acquisition and Stock*, 207 I. C. C. 641, 643; *Chicago G. W. R. Co., Trustees' Acquisition*, 230 I. C. C. 349; *Jefferson & N. W. R. Co. Acquisition and Operation*, 217 I. C. C. 483. This Court has also held that a railroad subject to the Interstate Commerce Act and in operation, desiring to enter into a trackage agreement to operate over the line of another railroad also in operation in interstate commerce, may not do so unless it first obtains a certificate of convenience and necessity under the provisions of Section 1 (18). *Transit Commission* v. *United States*, 289

U. S. 121. These decisions should have been accepted as controlling authorities requiring the Connecting Company to obtain a certificate prior to the resumption of operation of the line of railroad reverting to it upon termination of the lease.

The Commission predicated its ruling to the contrary primarily upon the theory that Debtor, the lessee, in operating the railroad did so as the agent of the lessor and that the latter, having received a charter and franchise from the State of New Jersey, is under an obligation pursuant thereto to operate the railroad.

It is submitted that the Commission's view that the Debtor was acting as the agent of the Connecting Company in the operation of the leased line of railroad cannot be sustained as a matter of law. A ninety-nine year lease represents a complete alienation of the possession and use of the property for the period of the lease; the only difference between a lease and a sale being that in the case of a lease there is a limit to the time during which the lessee may enjoy the benefits and obligations of possession. *Tiffany, Law of Real Property*, 3rd Edition, Sections 25, 76, 79 and 99. So long as the Debtor fulfilled the terms of the lease its possession and enjoyment of the leased property were complete and it was using the property for its own purposes and in no way acting as agent or *alter ego* for the Connecting Company.

Regardless of what may have been the relation between the Debtor and the Connecting Company it does not follow, as found by the Commission, that the Connecting Company is not required to obtain a certificate of convenience and necessity on the theory that it is under an obligation to operate the railroad pursuant to a charter and franchise issued to it by the State of New Jersey. The obligations of carriers under charters or franchises issued by states to

engage in interstate transportation may be enforced by the grantors only insofar as such enforcement does not conflict with the policy and laws of the federal government. By enacting the provisions of paragraph 18 of Section 1, Congress provided that whether corporations should be permitted to engage in interstate commerce by railroad is a matter to be determined by the Interstate Commerce Commission to the exclusion of whatever authority the states may previously have had. *Texas &c. R. R.* v. *Northside Belt Ry.*, 276 U. S. 475, 481; *R. R. Comm. of State of Cal.* v. *So. Pac. Co.*, 264 U. S. 331.

Moreover, it is to be borne in mind that if in the situation with which we are presently concerned the State of New Jersey were to refrain from enforcing whatever are the obligations of the Connecting Company to operate under the charter and franchise issued to it, the Connecting Company could under the Commission's theory, by refusing to operate, deprive interstate commerce of the services of the railroad owned by it. Considering that Section 1 (18) prohibits carriers from engaging in interstate operations or discontinuing such operations without first obtaining from the Commission a certificate authorizing them to do so, it is difficult to conceive that Congress intended any such exception to these requirements.

It is respectfully submittted, therefore, that the decision of the Commission in dismissing the application of the Connecting Company, thereby permitting it to engage in interstate operations without first obtaining a certificate of convenience and necessity under Section 1 (18) of the Act, rests upon an erroneous conception of the law.

In view of the obvious inconsistencies between the decision of the Commission rendered on the application of the Connecting Company on the one hand and the provisions of Section 1 (18) and the previous decisions of the Com-

mission and of this Court, the District Court should not have accepted the Commission's decision as *conclusive* evidence that the requirements of the laws relating to the continuous operation of the railroad had been complied with. The District Court should, under the circumstances, either have refused to accept the interpretation of the Commission or directed the Trustee to seek a review of the Commission's Order dismissing the application of the Connecting Company with the view of obtaining a final determination by the courts as to the application of the relevant provisions of Section 1 (18). Only in the light of such final determination could it be said that the Court had before it *conclusive* evidence that the Connecting Company had fulfilled the requirements of the laws as to the continuous operation of the railroad.

Point V

The District Court Erred In Permitting The Trustee To Discontinue Operation Without Prior Approval By The Interstate Commerce Commission Authorizing Such Discontinuance.

Section 1 (18) further provides that:

> "* * * no carrier by railroad subject to this part shall abandon all or any portion of a line of railroad, or the operation thereof, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity permit of such abandonment."

The effect of the decision of the District Court permitting the lessor to terminate the lease and to require the lessee to deliver possession of the railroad to the lessor will, if ultimately affirmed, have the effect of compelling the Trustee to discontinue operations notwithstanding that such a result would be contrary to the above-quoted provi-

sions of Section 1 (18) and certain of the provisions of Section 77. Congress, in enacting the latter section, very carefully provided that lines of railroad were not to be abandoned without prior approval by the Commission. Thus Section 77(o) (Title 11 U. S. C. A., Section 2050) provides that trustees may abandon lines or portions of lines of railroads upon petition to the Judge "but only with the approval and authority of the Commission when required by Chapter 1 of Title 49, as amended February 28, 1920."

Section 77(c)(6) provides that where a lease is rejected the lessee, under the circumstances set forth therein, may be required to continue to operate the leased line of railroad on or for the account of the lessor until the abandonment of such line is authorized by the Commission.

Reading the provisions of Sections 1(18) and 77(c)(6) and 77(o) together, it seems clear that it was the intention of Congress to prohibit the abandonment of any line of railroad by the Trustee without the prior approval of the Commission. This view is consistent with the conclusions reached by the Commission in several cases in which it has held that lessees of lines of railroad may not discontinue operations without its prior approval, as required by the provisions of Section 1(18). *Lehigh Valley R. Co. Abandonment of Operation*, 202 I. C. C. 659; *Norfolk S. R. Co., Receivers Abandonment*, 221 I. C. C. 258; *Duluth & I. R. R. Co. Control*, 224 I. C. C. 353.

We respectfully submit, therefore, that the Court should have directed the Trustee to apply to the Commission for authority to abandon the operation of the leased line of railroad prior to requiring him to deliver possession of the railroad to the lessor. In *Palmer* v. *Massachusetts*, 308 U. S. 79, 87, 88, this Court said:

> "The judicial process in bankruptcy proceedings under § 77 is, as it were, brigaded with the administrative process of the Commission. From the re-

quirement of ratification by the Commission of the trustees appointed by the court to the Commission's approval of the court's plan of reorganization the authority of the court is intertwined with that of the Commission. Thus, in § 77(c) and § 77(o) *the power of the district courts to permit abandonment is specifically conditioned on authorization of such abandonments by the Commission.*" (pp. 87, 88.) (Italics ours.)

For the foregoing reasons it is submitted that the failure of the Court to require the Trustee to obtain authorization from the Commission to abandon operation of the leased line of railroad is fatal to the validity of the Court's Order authorizing the lessor to terminate the lease and requiring the Trustee to deliver possession of the property to the lessor.

Conclusion

For the foregoing reasons we respectfully submit that the Circuit Court of Appeals in affirming the District Court's Order No. 39 has decided important questions of federal law which have not been but should be settled by this Court.

Wherefore, it is respectfully submitted that the writ of certiorari prayed for should be granted.

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Dated: August 30, 1945.